Internal Revenue Service
memorandum
CC:EL:D:4434-94
Br4:JSchwartz

date: FEB 7 1995

to: Assistant Commissioner (Examination) CP:EX

from: Assistant Chief Counsel (Disclosure Litigation) CC:EL:D

subject: Pro Forma Letter Used in Obtaining Information from the Securities and Exchange Commission (SEC)

This is in response to your request that we review the pro forma letter SEC requires agencies to use when requesting investigatory and non-public information from the SEC, and provide an opinion whether the letter can continue to be used without creating a conflict with and potentially violating the provisions of I.R.C. § 6103.

In your request, you mention that the SEC informed you that the issue was raised in the mid 1980's, that the pro forma letter was revised in 1987, and that the SEC believed it was reviewed and approved by this office. This office addressed the issues raised by the pro forma letter in 1982, and had some concerns regarding its use, as set forth more fully below. We do not have any record of having reviewed or approved a revision in 1987.

BACKGROUND

The pro forma letter assures the SEC that after receipt of requested information the IRS will: notify the SEC of any transfer to and use of the information by criminal law enforcement authorities or self-regulatory organizations subject to IRS oversight; make no public use of the information obtained without the prior approval of the SEC, and; notify the SEC of any legally enforceable demand for the information and will not grant any such demand without prior notice to, and lack of objection by, the SEC. The question addressed here is whether these notification and approval requirements conflict with, and potentially violate the confidentiality and disclosure provisions of I.R.C. § 6103.

In considering your particular request, we have determined that the IRS may be entering into similar use restriction agreements with other agencies.[1] In view of this,

[1] In fact, the use restriction language contained in the pro forma letter to the SEC is identical to the language found in IRM 9781, Handbook for Special Agents, Exhibit 300-36, Access Request by Federal Agency Other Than a Financial Institution Supervisory Agency. This exhibit is a letter to the SEC requesting access to investigative and other non-public SEC files. We are also attaching for your information a copy of a

you may wish to utilize the analyses and conclusions which follow in evaluating the issue of use restrictions by the IRS on a more global level.

CONCLUSION

The use restriction in the pro forma letter, which amounts to a limitation on disclosure by the IRS of information obtained from the SEC, and a blanket promise to contact SEC and in specified instances seek approval of disclosure of the information outside the IRS, is, in some circumstances, contrary to I.R.C. § 6103.[2]

LEGAL ANALYSIS

In your request for advice, you explain that the information is requested from the SEC for use in an official tax examination.[3] Once the information is received by the IRS in connection with an official tax examination, the information is tax return information

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memorandum of Understanding between the IRS and Customs. Your attention is directed to the third full paragraph on page six.

[2] An IRS commitment to SEC to comply with I.R.C. § 6103 would pose no conflict with or potential for violating the statute. Such a commitment would guarantee that the SEC information in the IRS' possession is protected tax information, statutorily mandated to be safeguarded from improper disclosure, the unauthorized disclosure of which is subject to civil and criminal penalties.

[3] It is possible that information can be sought and received from the SEC without the disclosure of tax information by the IRS. However, if it is necessary to disclose tax information to the SEC in order to obtain information from that agency, the authority for disclosing the information to the SEC necessary to obtain information from it is likely to be I.R.C. § 6103(k)(6) which provides:

> an internal revenue officer or employee may, in connection with his official duties relating to any audit, collection activity or civil or criminal tax investigation or any other offense under the internal revenue laws, disclose return information to the extent such disclosure is necessary in obtaining information, which is not otherwise reasonably available, with respect to the correct determination of tax, liability for tax, or the amount to be collected, or with respect to the enforcement of any other provision of [Title 26]. Such disclosure shall be made only in such situations and under such conditions as the Secretary may prescribe by regulation.

See also Treas. Reg. § 301.6103(k)(6)-1.

within the meaning of I.R.C. § 6103(b)(2). As such, the information in the possession of the IRS is afforded the protections of, and subject to the disclosure requirements of, I.R.C. § 6103.

Due to the use restriction in the pro forma letter, the question then becomes whether the IRS can legally refuse to disclose tax information if such information is requested by the President, Congress, the taxpayer, or any other person seeking such information, in accordance with the applicable provisions of I.R.C. § 6103 or other disclosure provisions of the Internal Revenue Code.

The primary reason for the enactment of I.R.C. § 6103 was to provide a statutory prohibition against unnecessary disclosure of returns and return information. The basic prohibition is contained in I.R.C. § 6103(a), which declares that returns and return information shall not be disclosed unless disclosure is authorized by some section of the Internal Revenue Code. Subsections (c) through (o) specifically authorize disclosure, as well as in some cases, require disclosure so long as the conditions set forth in the statute are first met. Those subsections requiring disclosure create a mandatory, not discretionary, duty. The subsections requiring disclosure relate to the following types of disclosures: subsection (d) - disclosure to state agencies for tax administration purposes; (f) - to congressional committees or their designees; (g)(1) - to the President or designated White House employees; (h)(1) - to Treasury Department employees for tax administration purposes; (h)(2) and (h)(3) - to Justice Department employees for tax administration purposes; (i)(1) and (i)(2) - to other federal agencies in connection with non-tax criminal investigations; and (i)(7) to the General Accounting Office (GAO) for use in certain audits.[4]

Because the provisions of I.R.C. § 6103 mentioned above require disclosure, the IRS is legally obligated to release to the requester tax information requested in compliance with these provisions. The IRS' agreement to be bound to restrictions on the use of information obtained from the SEC cannot override the duty to disclose such information as imposed by I.R.C. § 6103.[5]

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[4] Subsections 6103(d), disclosure to state agencies for tax administration purposes, and (i), disclosure for the administration of non-tax criminal federal laws and to GAO, also provide exceptions from the disclosure mandates. They allow the withholding of tax information if the IRS has determined that disclosure would identify a confidential informant or seriously impair any civil or criminal tax investigation. However, this exception from disclosure is narrow, and could not be relied upon to protect the document and information management concerns of the SEC.

[5] Other mandatory disclosure provisions which could potentially arise include section 6103(j)(3) - to Treasury for statistical purposes; section 9706(d)(2) - disclosures to Health and Human Services pertaining to certain beneficiaries in the coal industry; section 5021(c)(1) of Pub. L. No. 100-647, as amended by Pub. L. No. 101-239 - Alaska Native Corporation.

The use restriction specifically states that the IRS will:

> make no public use of the files or information without prior approval of [the SEC].
>
> notify [the SEC] of any legally enforceable demand for the files or information prior to complying with the demand, and assert such legal exemptions or privileges on [SEC's] behalf as [SEC] may request; and
>
> not grant any other demand or request for the files or information without prior notice to and lack of objection by [SEC's] staff.

This office specifically reviewed and commented on the use restriction in 1982 when we looked at this issue. It does not appear as though anything regarding the use restriction has changed since that time, and our analysis, therefore, is the same.

If the use restriction is given its literal reading, such that SEC reserves the right to approve or disapprove of IRS' intended disclosure of its information, then the use restriction would be in conflict with those subsections of I.R.C. § 6103 (listed above) which mandate disclosure. The IRS cannot agree to SEC's use restriction which conditions the IRS' mandatory disclosure obligations on SEC's consent.[6]

In addition to the above, the use restriction notification requirement raises a second disclosure question. The use restriction contemplates a disclosure by the IRS in order to solicit SEC's approval for disclosure of information previously furnished to IRS by SEC. To the extent such disclosure by IRS involves a disclosure of return information, the disclosure could be in violation of I.R.C. § 6103. Two situations come to mind: (1) if the IRS wanted to refer a tax case to the Department-of Justice's Tax Division pursuant to I.R.C. §§ 6103(h)(2) and (h)(3); or (2) if the IRS wanted to make investigative disclosures to third parties in the course of an investigation pursuant to I.R.C. § 6103(k)(6).[7]

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[6] When this issue was reviewed by this office in 1982, we were informed that the use restriction is not statutorily mandated, but is based on a policy decision by SEC. We do not have any evidence before us to indicate that this has changed.

[7] Additionally, the disclosure to SEC to secure its approval could be in violation of I.R.C. § 6103 if the IRS wanted to disclose information to the taxpayer pursuant to I.R.C. § 6103(e)(7). When we first reviewed this issue, we were informed that SEC's use restriction did not contemplate notification to SEC where the IRS discloses such information to the taxpayer. We assume, for purposes of this memorandum, that this is still the case.

Under the proposed agreement with SEC, the IRS would notify SEC of the intended disclosure and request its approval. From the proposal, it is unclear what information the IRS must give SEC to get its approval. It is not clear whether the IRS could simply ask SEC for disclosure approval, without specifying that the intended disclosure is to, for example, the Department of Justice for use in a tax case or to a third party in the course of a tax investigation, or whether the IRS must inform SEC to whom the disclosure is to be made and for what purpose. If the latter is the case, the notification informs the SEC of the fact of an investigation, which it may not have previously been aware of when the information was initially requested, as well as details of the IRS' investigation, both of which are included in the definition of return information.

There is no provision in I.R.C. § 6103 or other Internal Revenue Code section that would clearly permit the disclosure of this tax information to SEC. An argument could be made that I.R.C. § 6103(k)(6), authorizing disclosures for investigative purposes and discussed briefly earlier, would authorize the disclosure of tax information to SEC in order to comply with the terms of the use restriction. Literally read, I.R.C. 6103(k)(6) (See footnote 1 for statutory language), permits disclosures necessary to obtain information. In the situation presented by the use restriction, however, IRS would be disclosing tax information only to obtain approval from SEC to use information already received from them. Thus, the disclosure to SEC would not be made to receive "information otherwise not readily available ..."

Notwithstanding this literal construction of the statutory provision, it might be suggested that I.R.C. § 6103(k)(6) contemplates the disclosure of tax information in order to secure information which can be effectively used in the tax investigation for which the information was sought. It is an anomalous result for I.R.C. § 6103(k)(6) to authorize, in the first instance, a disclosure of tax information in order to initially obtain information from SEC, but then, in the second instance, prohibit the effective use of the information obtained by the IRS in furtherance of the investigation. In essence, it is possible that I.R.C. § 6103(k)(6) may be read to authorize the secondary disclosure to carry out the purpose of the primary disclosure.

[redacted]

[8] Section 6103(k)(6) disclosures are subject to frequent litigation under section 7431, which provides taxpayers with money damages in the event of unauthorized disclosures.

If the IRS need only inform the SEC that information previously received from SEC is to be disclosed to a third party, with no mention or explanation of the reason for the disclosure, an argument could be made that the IRS was not disclosing any tax information to the SEC.

Similarly, information concerning intended disclosures not relating to the investigation or prosecution of specific tax cases would not necessarily constitute tax information. For instance, a request for disclosure submitted by the White House which satisfies the requirements of I.R.C. § 6103(g), would not in itself constitute tax information, and the IRS could therefore disclose to SEC the fact that the IRS is considering release of the SEC information to the White House. See Tax Reform Research Group v. Internal Revenue Service, 419 F. Supp. 415 (D.D.C. 1976).[9]

In seeking approval, therefore, the IRS could furnish SEC with only the minimum information (i.e., that the IRS was considering disclosing the information furnished by SEC). Although the information provided to the IRS by SEC would constitute tax information in the IRS' possession, it could be argued that I.R.C. § 6103 would not come into play in this situation. There would be no disclosure since there would be no imparting of this information to SEC, merely the fact that information SEC previously provided may be disclosed.

In the context of disclosures under I.R.C. §§ 6103(k)(4) and (i)(1), the notification/approval requirements of the SEC's use restrictions present unique disclosure problems. Section 6103(k)(4) authorizes the disclosure of returns and return information to a "competent authority of a foreign government which has an income tax or gift or estate tax convention, or other convention or bilateral agreement relating to the exchange of tax information, with the United States, but only to the extent provided in, and subject to the terms and conditions of, such convention or bilateral agreement." Some conventions and bilateral agreements contain secrecy clauses under which the IRS has interpreted the tax treaties to preclude disclosing even the fact that a request for tax information by a competent authority has been made. As such, notification to SEC that IRS intends to disclose its information pursuant to I.R.C. § 6103(k)(4) may be a breach of the secrecy clauses of the tax convention or bilateral agreement.

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[9] A request for disclosure submitted by the Chairman of the Committee on Ways and Means, which satisfies the requirements of I.R.C. § 6103(f)(1), would not in itself constitute tax information, and the IRS could similarly disclose to SEC the fact that the IRS is considering release of SEC information to Congress. However, it should be noted that requests from the Ways and Means Oversight Subcommittee often include a statement that the request is a Congressional record which is not to be disclosed without the prior approval of the Subcommittee. Congressional requests of this nature would thus add an additional disclosure complication.

Section 6103(i)(1) requires the disclosure of returns and return information to the Department of Justice for federal non-tax criminal purposes, upon issuance of an ex parte order. By virtue of the ex parte proceeding, only the IRS and Department of Justice are aware of the order requiring disclosure. To the extent the IRS would have to notify SEC of the I.R.C. § 6103(i)(1) disclosure, it would be undercutting the policy of confidentiality of the ex parte order. Disclosures to SEC may create problems for the IRS in that the Department of Justice considers its I.R.C. 6103(i)(1) requests to be confidential..[10]

In conclusion, the IRS cannot ignore statutorily mandated disclosures of tax information simply because SEC does not give its approval for the disclosure. Furthermore, although there are situations in which the IRS may be able to notify SEC of the fact that it intends to disclose information received from the SEC, in those situations where the details of the proposed disclosure constitute tax information, the IRS could only provide such details to SEC as authorized by I.R.C. § 6103.[11]

If you have any questions, please contact Julie C. Schwartz of this office at 622-4570.

___/s/ John B. Cummings
(for) PETER V. FILPI

Attachment:
As stated

cc: Acting National Director, Intergovernmental and External Relations PC:E
Office of Disclosure CP:EX:D

[10] It is our understanding that on occasion, section 6103(i)(1) orders may be sealed, which would create additional problems in notifying the SEC.

[11] We would also note that there may be a Privacy Act issue in the situation where the IRS intends to disclose information received from the SEC pursuant to section 6103(l)(4) in connection with personnel actions. Notifying the SEC that their information is being disclosed in this context may reveal the fact of a personnel action involving a particular individual. There would first have to be a routine use to authorize the disclosure of such information to the SEC pursuant to subsection (b)(3) of the Privacy Act. 5 U.S.C. § 552a(b)(3).